BUSINESS CREDIT BEST BASIS FOR SOUND BANKING

(Continued From First Page.)

which will inquire into and find out the use to which the proceeds of plans are put, and which will keep the officers who make loans supplied with information which will enable them to know how a prospective borrower will use funds put at his disposal.

Danger of Inflation.

Unfortunately banks conducted according to this plan are rare. Most bankers are not aware of the importance of the distinction between these two kinds of banking. Their inquiries regarding loans are usually limited to the security back of them. If they are satisfied that the man or men whose names are on the paper they buy are good for the amount borrowed, they consider the loan good, and take it without hesitation, blissfully unconscious of the fact that a good loan for an investment banker may be a very bad one for the commercial banker, bad not necessarily in the sense that it will not ultimately be paid or even in the sense that it may cause trouble immediately to the banker who makes it, but in the sense that such loans, if they exceed in the aggregate the bank's capital, surplus and genuine savings deposits, are certain to result in inflation and to contribute to the evil consequences of such a condition.

Inflation is a much used but imperfectly comprehended term. It is a word to conjure with rather than one which brings before the mind of the person who uses it a perfectly definite financial condition. It is therefore badly in need of explanation in this connection.

It describes the state of the commercial banks of a country when they have created against themselves as a group obligations which they are unable to meet in the normal course of their business. The characteristic business of a commercial bank is the exchange of its obligation to pay on demand for the obligation of others to pay in the future. Its ability safely to conduct this kind of business depends upon the strict limitation of its operations to the processes of bookkeeping mentioned above. If the debits and credits it registers on its books balance, or so nearly balance that the difference between them can easily be met by the cash that normally circulates in its community or which it can attract from other communities by normal methods, no difficulty can arise, but, if the differences are greater than this, extraordinary and painful methods of adjusting them are necessary, methods which always result in financial loss to large numbers of people and frequently in commercial and financial crises.

Tying Up Liquid Capital.

Now precisely this condition of things is produced when commercial banks purchase investment securities in excess of the amounts of their capital, surplus and genuine savings deposits. If they create demand obligations against such securities and their payment is demanded before such securities mature, they will have no funds to meet them, and no funds can be procured unless such securities can be unloaded on other banks at home or abroad. They cannot be unloaded on other banks at home because by hypothesis, as a group, home banks are in the condition described and they can only be unloaded on banks in other countries at such a time as such banks decide to impose.

The situation is entirely different when commercial banks create demand obligations against commercial paper only. Such paper represents current purchases and sales which, being offset against each other in the form of debits and credits on the banks' books or in the form of the cash that goes out and return in the payment of maturing paper, make no demands which the banks are unable to meet.

It is obvious that inflation may occur either in the note issues or in the checking accounts of commercial banks and that it bears no relation to the magnitude of either or both. Provided they represent actual exchanges of goods they may be expanded to any desired extent without inflation, but to the extent that they represent one-sided transfers of goods, as they always do when banks create demand obligations against investment securities, inflation is the result no matter how small is their magnitude. Of course great inflation is worse still than slight inflation, but the quality and character of it is the same in both cases.

When inflation occurs, forced liquidation is the only alternative. This takes the form of the forced sale of securities by banks or their customers and the cutting down of loans which results in forced sales of many other forms of property. If these forced sales are so great in amount that the markets cannot provide for them, failures and settlements through bankruptcy and other court proceedings follow, and such a condition is likely to be accompanied by a commercial crisis.

Bank Note Inflation.

That inflation in varying degrees of magnitude, caused by the combination of commercial and investment banking, characterizes the finances of the United States the greater part of the time will become evident to any one who carefully follows current events in the financial world and analyzes our currency situation. In the first place our issues of national bank notes against government securities produce inflation to the extent that [illegible]

This condition of things does not necessarily, and usually does not, take the form of the presentation of these notes for redemption. Being as good and as convenient as any other form of hand-to-hand money, they are likely to remain in circulation, but only at the expense of other forms of money, frequently of gold, which [illegible] are more easily displaced. The forced liquidation really occasioned by them, therefore, [illegible] likely to take the form of the export of gold, [illegible] however, take the form of the export for the payment of [illegible]

demand obligations which the banks have assumed.

Our seasonal monetary stringencies and frequent high loan rates are chiefly evidences of inflation. It is because banks are forced to take extraordinary measures to meet the demand obligations they have assumed, and are forcing liquidation on their customers that these phenomena occur. They would not be forced to take such measures if their operations had been confined to purely commercial lines, or if they had not tied up commercial funds in investment securities.

Funds Flow to Wall Street.

Our reserve system is a constant invitation to inflation and forces it at times. The balances which banks keep with their reserve agents can only be used by operators on the New York Stock Exchange and, while speculation in ordinary times renders these balances extremely liquid, at other times, when it misjudges the resources and the inclinations of the investment market, they are very far from liquid and produce inflation in an extreme form. Another portion of our bank reserves, the so-called secondary reserves, are of necessity invested under our system in high grade bonds, which, like call loans based on stock exchange collateral, are easily disposed of so long as investment funds are in the market in sufficient quantities, but unsalable when such funds are exhausted. If at such times banks hold securities against their demand obligations, inflation is the result.

The prevention of the confusion of commercial and investment banking and of the inflation which results therefrom is not a simple problem. The first essential to its solution is the general recognition of its existence by bankers and their customers. So long as both parties feel, as they do now, that any man with good credit and good security is entitled to a loan from a commercial bank regardless of the purpose for which the funds are to be used, there is little hope. On the other hand, a perfect understanding of both parties that only funds destined by their owners for permanent investment should be loaned for the purchase of lands, the construction of houses, the building of factories and their equipment, the digging of mines, the construction of railroads, canals, etc., etc., and that those funds which represent the circulating capital of the community should be loaned for commercial purposes only, would predispose the public to search for such modifications in our banking system and methods as would make the separation of commercial and investment banking easy, and properly to use the necessary financial machinery when it is supplied.

National Market for Commercial Paper.

The next step must be the creation of a national market for commercial paper. At the present time the bulk of the paper which ordinary commercial processes bring into existence can be marketed at the local bank only, since the maker of this paper is unknown beyond the locality in which he lives. What we need is the machinery for giving such paper, when it is first class, nation-wide currency, so that the local banker's ability to discount will not be confined to the resources of his own community, if they are limited, and so that he can safely discount his paper in other communities if his necessities exceed local needs. This end attained, bankers' balances with reserve agents would not need to seek the New York stock market for employment and secondary reserves could be made up of commercial paper instead of bonds.

Before we can have a national discount market we must create a central institution for the purchase of amply secured commercial paper and equip it with the means of making such purchases in whatever quantities may be necessary. For such equipment there are two essentials: it must hold the cash reserves of the entire country, that is, the country's supply of gold, or that part of the nation's supply of cash [illegible] as a medium of exchange, and it must have the right to issue notes against commercial assets. As the custodian and administrator of the nation's central money reservoir, it would become the centre of its commercial bookkeeping machinery, balancing on its books the mutual indebtedness of all other institutions, reducing the use of money to the minimum and giving maximum efficiency to our money resources. The right to issue notes against commercial assets would enable it to supply the necessary elastic element in our currency and to reserve an adequate supply of cash for international and emergency uses.

Value of Bank Acceptances.

A very important though not absolutely essential adjunct to a national discount market is the right of banks to accept bills for their customers and the development of the practice of making such acceptances [illegible]

GREAT NATIONAL CORN EXPOSITION

(Continued From First Page.)

perience how to estimate the value of undeveloped opportunities. It will pay the farmers of Virginia to get in touch with them when they come to Dixie. They are ready to teach and they are ready to be taught. Southerners can learn of them and they should learn of Southerners.

The Boys Will Be There.

"It has been the policy of the management to broaden the scope of the exposition each succeeding year," writes Mr. Brunson. "While the fifth exposition will be conducted along the same general lines as the fourth, a number of new features will be introduced. One of the most striking of these will be the first exposition school for boys, which will be composed of the prize winners in the boys' corn clubs in every county in the Southern States and in a number of the Northern and Western States. The attendance upon this school is expected to reach at least 1,000. It will be characterized by semimilitary discipline. To make this unique institution a success from all standpoints, the boys' department of the Federal Farm Demonstration Work is co-operating with the exposition management, and State and county agents throughout the South, together with county superintendents of education, are working actively in its behalf.

"A number of other features, attractive through their novelty, as well as substantial in character, are being planned for by the exposition management.

"This is the first time the National Corn Exposition has been held in the South. Its standing before the country is already established. Farmers of every Southern State, and all others who are interested in the advancement of the people, have ahead of them a great educational privilege, and as many of them as possible should take advantage of it.

TOBACCO SCRAPS FROM TWO STATES

(Continued From First Page.)

—whose ancestor founded the business.

Well, that makes it all the better for the Virginia cigarettes, about all of which are made in Richmond.

The Southern Tobacco Journal says: "The 1912 South Carolina tobacco crop has long since passed into history. The crop in Eastern North Carolina is practically all out of the hands of the farmers. The Old Belt markets in North Carolina and Virginia report crops from 75 to 85 per cent sold. The crop is moving in the West as rapidly as seasons will permit. Summing up the whole situation, we are sure that the crop will be out of the farmers' hands earlier than ever before. Hundreds of tobacco farmers are already making preparations for another crop."

Many Virginia and North Carolina country people living near the leaf tobacco markets of the two States earn pretty good purses every year making and selling the broad tobacco baskets. This home industry seems to be expanding, and the demand is now greater than the supply. The Tobacco Journal thus explains:

"What causes the great demand now is that thousands of baskets are shipped to the West. Tobacco on the Western markets is unloaded and placed on the warehouse floors in baskets. This system not only necessitates a great many baskets, but they wear out very rapidly."

The warehouses of Chase City have sold more leaf within the past three months than in any similar period in the history of the market. Chase City is both a bright and dark market.

The drakes Branch market handled over a half-million pounds of the leaf the last sales week in this month.

South Boston still has its pins set for 25,000,000 pounds of the bright goods for this tobacco year, and the market has good prospects to reach the height of its ambition.

Now that no taxpaying whiskey or brandy distilleries exist in North Carolina, Winston-Salem claims that over 90 per cent of the internal revenue of the Western North Carolina district is paid to the government by the tobacco manufacturers of that town. Therefore the headquarters of that district should, by rights, be located in Winston-Salem.

GRAVITY SAFETY SIGNAL.

[illegible]

Remington's New Bank.

[illegible]

Richmond Man In It.

[illegible]

TENDENCIES THAT ARE FUNDAMENTAL

Financial and Industrial Conditions and Their Explanation. Increased Pressure

(BY W. J. LAUCK.)

Land as a productive factor is limited in extent. It consists of that portion of the earth's surface which may be used to produce cereals and other commodities for man's sustenance. Even that portion, however, of the land available for the cultivation of certain crops is of varying degrees of fertility. The price of any agricultural product is, therefore, determined by the cost of production upon the poorest land, which must be utilized to produce the necessary supply. In this fact we have the fundamental explanation of the rise in the level of prices and the general cost of living. During the past half century, large industrial communities have come into existence, and for various reasons the tendency has been for population to concentrate in urban districts. No better illustration of this tendency can be found than in the recent development of the South. With the establishment of mining and manufacturing communities, areas of farming land have been left vacant or only partially cultivated because the movement of the agricultural population into the cities and towns. The world-wide tendency in this direction has been offset in the past by the adoption of better farming methods and by the invention and use of improved agricultural machinery. Within recent years, however, the land has not been able to respond to the increasing demands made upon it by the industrial, the commercial and the non-productive parts of the world's population. As a consequence, the prices of agricultural products have risen rapidly. Recourse to lands of inferior fertility in order to produce the required supply of foodstuffs has caused a diminishing return to the labor and capital invested and a further enhancement of prices. More extensive cultivation will only serve to intensify this tendency for prices to rise. Relief must be found in the elemination of waste in consumption, in devising better methods for marketing farm products and in working out and adopting economical methods for the intensive cultivation of the soil.

Depreciation in Gold.

To these basic tendencies in the production of foodstuffs should be added another fact of primary importance in its effect upon prices. During the past twenty years there has been an extraordinary increase in the world's gold supply. The remarkable rate at which the available quantity of this precious metal has been increased may be quickly seen from the statistics relative to annual output. In 1885, the output of the mines of the world was only $108,000,000, as contrasted with $288,000,000 in 1910, the latest year for which statistics are available. As the value of gold is determined by the same factors as that of any other commodity, the unprecedented increase in the supply within a comparatively short period of time has tended to cause a decline in the value of gold as compared with other commodities. This tendency has been largely offset by the increased demand for gold in the arts, for monetary purposes, and for use in banking reserves because of the rapid expansion of the world's credit structures. Despite these counteracting circumstances, it is probably true that gold has undergone some depreciation in value, and, as gold is the world's standard of payments, both present and deferred, the result has been that more gold is now required than formerly to purchase other commodities. In other words, the prices of other commodities, as well as the interest on capital, have tended toward a higher level because of a tendency towards a decline in the value of gold, in which prices are expressed.

These two facts—the pressure of population upon the land and the remarkable increase in the world's supply—afford the fundamental explanation of the general advance in prices in all countries of the world within recent years. In the United States the level of prices has been higher than in other countries because of tariff favors and other special legislation, which have given a monopoly control over prices to favored interests. Waste and extravagance in living have also intensified the effect of fundamental conditions. Several other factors, comparatively of minor importance, as well as the bearing of the other productive factors—labor and capital—upon the creation and distribution of wealth must be considered, before the existing financial and industrial situation is fully appreciated.

Labor as Productive Factor.

The productive factor, labor, consists of that part of the population which is engaged in the creation of goods or wealth. It increases in geometrical ratio and tends to outrun the means of subsistence which only increases in arithmetical ratio. Its share of the output of industry is determined by its bargaining power in dealing with capital. This strength, in negotiating with the capitalist or manager of modern industry, through whom the demand for labor is expressed, is conditioned upon the character of the labor supply and upon the extent to which the supply is organized for collective action. The lowest rate of wages must be equivalent to a subsistence level, the general rate usually is representative of a generally accepted standard of living, and the maximum rates, as a rule, are determined by the degree of efficiency of the workmen, or by their monopoly control of certain classes of the supply. The rates of pay tend to correspond to the movements of the prices of commodities, although prices usually rise first. Manifestly, at any time, the surplus of labor above the cost of living is dependent upon the inclination and opportunity for saving.

Accumulations of Capital.

The remaining factor in creating wealth is capital, which, although expressed in terms of money, in reality consists of machines, buildings and all other instruments which are the product of past labor, and which are designed to be used in further productive processes. Capital, in other words, is the tool which successive generations of labor have made to facilitate the world's undertakings. Capital is freely reproducable. The increase in the supply has only two limitations—the extent of the surplus remaining from the world's production of wealth after the economic wants of man have been satisfied, and, upon the degree of the inclination among men to refrain from undue consumption and to devote a portion of their present surplus of wealth to the production of future wealth. War and similar devastations, or an act of nature may destroy part of the world's accumulation of capital. The present Balkan conflict and the recent earthquake at San Francisco, or the sinking of the Titanic may be cited as illustrations of such catastrophies.

An analysis of existing economic conditions in the light of these fundamental facts, and of the origin and characteristics of the basic productive factors, discloses some exceedingly significant tendencies. The steady rise in the price level caused by the increasing pressure upon the land and the depreciation in the value of gold has brought about world-wide industrial unrest and labor disturbances. In order to maintain their accustomed economic standards in the face of an advance in the cost of living, there have been general demands from all classes of labor for increases in their rates of remuneration. The wage level has also failed to rise as rapidly as prices, and, consequently, the margin between consumption and earnings has grown steadily narrower and has left a decreasing amount available for accumulation. This tendency has been intensified by waste and extravagant methods of living among all classes of the population. The net result, therefore, has been a decline in savings bank deposits as compared with former years, or, in other words, new accumulations of capital by wage-earners and salaried workers has been proportionately smaller within recent years than in the past. Furthermore, the general rise of prices has also added to the costs of materials and machinery, and has left a smaller margin of profit to the capitalist and to the investor. Available additions to the existing supply of capital from these sources have, therefore, been declining as compared with former years.

Interest Rates and Demand for Capital.

Recently there also has been an increasing demand for capital. According to the London Economist, the new capital commitments in England in 1902 were only £159,358,500, as compared with £267,439,100 in 1910. In 1910 the listing of securities on the New York Stock Exchange for the purpose of securing new capital was $876,000,050, as against $750,000,000 in 1902. This diminishing possibility of accumulating new capital, however, because, as already pointed out, of the increasing cost of living and smaller profits, has caused the available supply of capital to fall behind the demand.

As a consequence, interest rates have risen, or, in other words, the borrowers of capital are compelled to make comparatively larger payments for its use. The advance in the rate of interest may have been slightly affected by a depreciation in gold, but the underlying cause has been a relative decline in the accumulation of new capital in the face of an increasing demand.

The general tendency in the industrial world has been to offset rising costs of manufacture by advances in price. This, of course, assumes the ability, to some extent at least, to control prices. The transportation companies of this country, of which the freight rates cannot be raised unless the Interstate Commerce Commission approves, afford the best illustration obtainable of the effect of present economic tendencies upon an industry which is unable to make a higher charge for its output. The operating expense of the railroads during the past ten years, owing to larger rates of remuneration to employes and the advance in the prices of materials and supplies, have steadily increased and have tended to lessen the amount of net returns. Although railroads have successfully endeavored to meet this situation by economies in operation, they now state that the maximum of efficiency has been attained, and the railroads must be granted the privilege of advancing their freight rates in order to maintain their credit. If this request is granted, as it may be, after serious consideration, it will have the effect of adding to the general tendencies bearing upon increased manufacturing, distributing and living costs.

Capital Commitments and Bank Resources.

Another discouraging feature of the present economic trend is to be found in the commitment of increasing proportion of capital into unprocuctive government and municipal loans, or into unproductive industries as exemplified by the extraordinary growth of the automobile manufacturing industry, or into forms which are more or less fixed and permanent and which are not quickly convertible. The land and building booms in the South at the present time, which, in some cases, are proceeding upon an inflated basis, are examples of this latter tendency.

The investment of capital into certain forms of speculative undertakings, such as the rubber industry, and the establishment of amusement facilities, has also been marked during recent years. The general inclination to use capital freely in long-time or unproductive enterprises, and to inflate the credit structure with the flotation of such undertakings, has also been attended in the United States by a period of liquidation since 1907. It has only been within the past year that freedom from the depressing effects of the panic of that year has become so noticeable, and it is generally conceded that we are not yet through with the payment of obligations created by that financial disaster.

What of the Future?

The bumper crops of the present year have brought about a pronounced revival in business and industry, and if we have a repetition next year of this unusual agricultural yield, it will place us a long way on the road to an extended period of prosperity. It is by no means certain at the present time, however, that our present prosperity will be more than temporary. The prospect of tariff reduction will have a favorable effect upon manufacturing costs and retail prices. The large gains in the resources of our banks during the past year is also encouraging, while the possibility of securing reforms in our defective national banking laws will be a decided advantage in any liquidation which is now in progress and is essential to the safe financing of future industry and trade. Safety and prosperity in the future is more dependent upon banking reform than any other factor. It is also certain that wastefulness and extravagance in private, corporate and public expenditures must be curtailed and our resources husbanded. Caution should also be taken against the creation of a credit structure based on inflated land or other values, and capital should not be too freely committed to fixed and unproductive forms. The pressure upon the land must also be relieved by a more economical and intensive cultivation of the soil, by the development of agricultural facilities and by the adoption of more inexpensive methods of marketing farm and manufactured products. Only by exercising such conservative methods and precautions, can business and industry hope to prevent a collapse in the present high level of prices and values and a consequent readjustment, before a period of permanent prosperity is assured.

REAL ESTATE AND BUILDING NEWS

(Continued From First Page.)

thoroughfares. During the year quite a number of residences on East Grace in the neighborhood of Sixth, Seventh, Eighth and Ninth have been tore down, or bought to betorn down, to make room for business houses. The same may be said of East Franklin in the same regions, and business keeps going right along up Main Street, until it has gotten among the residences of the small numbers of West Main.

Looking Ahead.

So much for the year that is dying and that comes in the way of a general review. And now what of the year ahead? All of the agencies predict that 1913 will leave 1912 in the shade by making a new record in the real estate line, and I must say that all the signs of the times point to that very thing.

The real estate business was a little slow during the past week, it being practically the last week of the dying year. The agents were content to busy themselves winding up the deals of the year, so as to start next Wednesday morning with a clean record. Nevertheless, several deals of large proportions that had been hanging on the string were closed up, and the prediction made in this column that there would be only a one day's let up was verified.

Phenomenal Building Operations.

The report of the Building Inspector for the year has not yet been completed, and in the nature of the case cannot be completed until Tuesday night. However, a glance at Inspector Beck's books and records reveal the fact that the structural growth of Richmond, both in its business and residential districts, has exceeded this year even the phenomenal record of 1911. It is certain that the final reports of the inspector for the year will show that Richmond has led all of the Southern cities in building construction for this year as compared with 1911.

The enormous increase in the volume of building operations here in 1911 was the subject of wide comment last January, when the statistics were published, Richmond's growth was pronounced phenomenal.

That record, however, will be broken by the figures for the year which will end next Tuesday. The figures already show a total expenditure for new work and repairs amounting to $6,122,481. At least 20 per cent may be added to the total, for applicants for building and repair permits are prone to underestimate the cost when filing plans for official inspection.

The total for 1911 was $6,018,699. The increase this year to date is therefore $104,782. The permits to be issued before December 31 may add substantially to the figures given to-day.

Of the $6,018,699 total for 1911, $5,474,289 was for new buildings and $544,410 for alterations and repairs to old structures.

The total for new buildings this year so far is $5,642,961 and for alterations and repairs, $507,412. It will be seen that less money was expended on old buildings than in the preceding year and more in new construction.

The year 1913 promises to open with considerable activity in building operations. Plans for several large and costly buildings are being prepared and will be submitted to the Building Inspector early in the year. Among the larger buildings projected are the Monroe Terrace Apartments, to cost more than $300,000, the new armory for the First Regiment, which will [illegible] skyscraper office building at Twelfth and Bank Streets.

Sawdust Sugar.

[illegible]